

An exempt organization's payment of reasonable pensions to retired employees at the discretion of its board of directors does not adversely affect its exempt status.

Advice has been requested whether the payment of pensions as described below affects the status of an organization exempt from Federal income tax under section 501(c)(3) of the Internal Revenue Code of 1954.

The organization carries out its charitable program through a staff of salaried employees. It has no established retirement plan for these employees but has followed a general practice of paying pensions to retired employees at the discretion of its board of directors. The recipients have no enforceable rights to payment. The pensions are not gratuities but represent extra compensation for past services, are reasonable in amount as compensation for such services, and would be deductible for Federal income tax purposes if incurred in the conduct of trade or business.

Section 501(c)(3) of the Code provides for the exemption from Federal income tax of organizations organized and operated exclusively for charitable purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

The payment of pensions to retired employees is an accepted method of employee compensation used by many public and private organizations. Since the payments for the pensions in this case are reasonable compensation in the light of the surrounding circumstances, they are a proper expense in the operation of the organization's charitable program and do not constitute the improper use of the organization's charitable resources, nor do they constitute inurement of the organization's net earnings to private individuals within the meaning of section 501(c)(3) of the Code.

Accordingly, it is held that the organization's payment of pensions to retired employees as described above does not adversely affect its exemption from Federal income tax under section 501(c)(3) of the Code.